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**PRESIDENTIAL ECONOMIC DELEGATION TO
POLAND—OVERVIEW AND EXECUTIVE SUMMARY**

COMMUNICATION

FROM

THE PRESIDENT OF THE UNITED STATES

TRANSMITTING

**FINAL REPORT OF THE PRESIDENTIAL ECONOMIC DELEGATION
TO POLAND IN NOVEMBER 1989**



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THE WHITE HOUSE,
Washington, DC, December 22, 1989.

HON. THOMAS FOLEY,
Speaker of the House of Representatives,
Washington, DC.

DEAR MR. SPEAKER: I am transmitting herewith the final report of the Presidential Economic Delegation that I sent to Poland at the end of November. I think that you will find the conclusions of Secretaries Yeutter, Mosbacher, and Dole and CEA Chairman Boskin, and of the 20 distinguished private sector participants in the Mission, well worth reading.

This report will help to ensure that the assistance provided by the "Support for Eastern European Democracy Act of 1989" will be used to maximum effect.

Sincerely,

GEORGE BUSH.

Presidential Economic Delegation

Overview and Executive Summary

Overview

The Presidential Delegation demonstrated to the Polish people in a highly visible way that their noble experiment has the enthusiastic support of the United States. As one man on the street put it to one of our interpreters, "The Americans are finally here!"

The mix of public and private sector participants worked well, fully succeeding in its purpose of blending healthy, hands-on free market experience with the skills of administering public programs in a democracy.

Several themes recurred repeatedly throughout the various sectoral programs into which the Delegation divided upon arrival:

--As we had thought, the Poles particularly appreciated our advice and offers of technical assistance (accounting, banking, marketing and management skills);

--The first order of business for the Poles will be macroeconomic adjustment of their economy, especially gaining control of their hyperinflation and achieving convertibility of the zloty;

--While the entrepreneurial spirit which has survived 40 years of state control, and the popular support for Poland's free market experiment are inspiring, quick positive results will be important in strengthening this support;

--In all areas, training in free-market approaches and skills will be critical for a workforce that has never operated in a competitive business environment.

--Foreign assistance, financial and other, must be on a sustained basis. The problem in Poland developed over a long time period and the restructuring will also take an extended period of time.

Assessment

1. Macroeconomic Analysis

Poland starts with great burdens: rampant inflation (50 percent monthly), a per capita GNP one-tenth that of the United States, a foreign debt equal to 60 percent of GNP.

The causes, hidden subsidies to inefficient state enterprises and huge budget deficits, are also clear. In such a situation, even elementary planning is complicated by the impossibility of making accurate economic assessments in all areas.

The prescription which the Poles have set for themselves is the correct one: reducing inflation, working down foreign debt, decontrolling prices, reducing subsidies and privatizing state companies to create a free-market economic system. The challenge will be in achieving all this at once with a small core team which has had little experience in operating within the environment it is striving to create.

2. Agriculture

Agriculture is critical to Poland's success for many reasons. It is the one economic sector already privatized, and one where the chances of an early turnaround are greater and would provide a visible early symbol of success. Agriculture employs 30 percent of the workforce, and people spend huge amounts of time procuring food. Clearly agricultural restructuring will liberate enormous resources for use elsewhere in the economy. For the United States, agriculture is an area where our technological leadership is unquestioned.

Food is more available in stores, but at high prices in this early stage of the necessary price adjustment that is taking place. On the farm, Poland stands good chances to be competitive in a number of staple and specialty crops and meat production, but only if farmers receive necessary inputs. Processing and distribution of both farm inputs and farm outputs are areas where necessary systems need to be built from the ground up. Management training is a necessary step toward achieving efficient processing and distribution of farm inputs and outputs.

3. Commercial/Industrial Sector

The state owns 90 percent of the industrial economy and its condition is poor: physical plant is old and obsolete in most industries. Both importation of machinery and development of more efficient production within the country are needed.

Polish leaders understand the nature of their problems in commerce and industry well, but the challenge facing them is very great. From almost no base, they need to construct efficient banking, telecommunications and

pollution control industries. Systems that in the West are taken for granted like accounting, commercial law and financial management are nonexistent in the sense that we know them.

4. Labor

Poland's attributes include a young, highly literate workforce which shares the enthusiasm of its leaders for economic and social change. Yet training is called for to enable these workers to prosper in a market economy.

Unemployment could be a critical problem during the economic transition, as there are significant barriers to worker mobility. Measurement of the situation is difficult, but in light of the widespread redundancies in state enterprises, job loss could be substantial as these entities are restructured or privatized. The introduction of free enterprise wage incentives, however, should make Poland's workers an important source of international competitive advantage as reform progresses.

Recommendations

1. Macroeconomics

What must be attempted is clear: controlling inflation and achieving a convertible currency will be critical to any success in other sectors. In this regard, the U.S. and G-24 initiative to provide a \$1 billion support fund is the appropriate response so long as that fund is used to support and not to postpone adjustment.

Training in many economic and professional skills is a must: banking, law, accounting, management of all kinds. Further, policy should be structured to encourage small, start-up businesses even as large state companies are broken into more manageable, efficient units. The United States can be helpful not only in training and technical advising, but should also study Poland's further credit needs as it restructures.

2. Agriculture

Public and private efforts should be undertaken to assure adequate feed and chemical inputs for the 1990 crop. This effort must be coordinated with our G-24 allies. It is likely that further U.S. food aid need be confined only to feeds.

In addition to announced food and feed aid, U.S. Government agricultural assistance will include the provision of \$20 million in soybean meal during calendar 1990, and increased training through the Cochran fellowship program. A team of U.S. extension specialists will make an early survey visit to study the weak Polish extension system. A USDA working group is being established to coordinate assistance that is available from that Department, and a governing accord with Polish Ministries was signed on December 16.

The U.S. private farm sector is studying several ways it may help. Corporate and academic extended work/study programs and a farmer exchange program are strong possibilities. Both will give Polish farmers and agribusinessmen hands-on free market experience. Private agribusiness coordination, for example direct linkages between producers' associations in the two countries, are also being studied.

3. Commerce/Industry

Early signing of the Comprehensive Business and Economic Agreement will provide a basis for increased U.S. investment. Technical assistance is likely to be targeted to several specific sectors including banking, mid-sized agricultural and industrial enterprises, telecommunications and pollution control.

The Enterprise Fund should begin operations promptly. Similarly, Commerce and related agencies should immediately plan informational seminars on the various resources made available to Polish business in the Support for East European Democracy bill.

Training is critical here as in other areas, and private sector exchange programs have a key role to play as does the International Executive Service which will place experienced personnel in Poland shortly. U.S. industry teams could offer much expertise in areas like privatization, coal exportation, pollution control, natural gas development and others. A Polish-American productivity institute, similar to the Japan Productivity Center, has potential in this area.

-5-

Poland should do its part too, for example through permitting 100 percent foreign investment ownership for demonstration projects.

4. Labor

The United States and Poland have already signed, and should move quickly to carry out, a Memorandum of Understanding on labor technical assistance. Areas covered include basic management and entrepreneurial skills training; assistance in implementing unemployment compensation and employment services systems; development of labor statistics; and housing industry crafts training in conjunction with the AFL-CIO.

The social aspects of economic reforms must be of continuing concern to the United States. A popular consensus for the government reform program is a prerequisite for economic success, so the Department of Labor -- in close cooperation with the AFL-CIO -- must continue the work begun by the AFL-CIO to support and build democratic institutions in Poland.

There is also a role for private voluntary agencies to help provide a basic "social shield" for those Poles most adversely affected by economic restructuring. Information on successful U.S. models of voluntary support services will be provided to Polish officials, and the Department of Labor (DOL) will work closely with volunteer service organizations in the United States to marshal the generosity of the American people in support of Poland's priority social needs. The authority that was sought by DOL and included in the SEED Act for the Secretary of Labor to solicit and accept gifts in support of the labor technical assistance program will be vigorously implemented to leverage federal resources available for this critically important component of the Administration's overall assistance program.

Macroeconomics and Finance

The government leaders we met with are convinced -- and appropriately so -- that market-oriented reforms are the only hope for major improvement in their economy. However, it is important that expectations not get too far out of line with what can be accomplished in a relatively short period of time and Poland's leaders are cognizant of this. The new government needs some short-term successes in getting more and higher quality goods on the shelves next year. It is recognized that Poland is a poor economy facing multiple challenges.

- o real GNP per capita in Poland is roughly one-tenth that of the United States;
- o inflation is over 50 percent per month;
- o foreign debts exceed 60 percent of GDP; and
- o the economy is outmoded and inefficient, the legacy of 40 years of central planning under Communist control.

A number of countries have successfully reduced inflation from high levels, others have worked off large foreign debt, decontrolled prices, sharply reduced subsidies or privatized state enterprises, but no country has solved all of these problems at once following 40 years of state planning.

The new government has developed a bold and comprehensive set of policies to reduce the inflation rate, to reform prices, to privatize state-owned enterprises, establish a private financial system that encourages saving and investment, and to carry out other structural reforms. Their highest priority is to quickly reduce the rate of inflation and establish a stable environment in which needed business reforms and foreign investment can take place. This will entail sharply reducing the large government and state enterprise budget deficits. It is important to move quickly to reduce inflation. The fundamental element in any disinflation program is reducing the budget deficit by cutting subsidies, especially to inefficient state enterprises whose deficits have been routinely covered by expanding the supply of money and credit. The Government of Poland plans to gradually introduce structural reforms and to begin privatizing selective state enterprises.

The overall plan is consistent and based on sound principles. There is a high degree of commitment to these

policies by the government and the Parliament. The broad steps are well understood, and the policies appear to enjoy a broad base of support, ranging from Solidarity to the Communists.

Poland faces major challenges in implementing these policies. The economic team headed by Finance Minister Balcerowicz has identified the policy measures needed to create market institutions, but the public and private sectors for the most part have little or no experience with Western market economies. The economy is outmoded and inefficient, the legacy of 40 years of central planning. The workers are relatively young and well-educated, but lack experience with incentives or the specific technological skills demanded in today's globally competitive environment.

The Poles must have ambitious, yet realistic, goals with sufficient flexibility to adjust as required on issues ranging from exchange rate policy to reducing subsidies and the budget deficit.

Reducing the rate of credit creation and money supply growth: One of the primary sources of the rapid rate of inflation has been to keep inefficient state enterprise afloat and to keep prices of essential goods low. Successfully cutting this credit creation while simultaneously reducing subsidies to state enterprises will not be an easy task. Some inefficient firms will clearly go bankrupt and require reorganization. Establishing a sound long-term credit policy will take time and will require the adoption of standardized accounting and credit appraisal techniques and a large increase in the number of trained professionals in these areas.

Reducing the Budget Deficit: The new government is relying mainly on cuts in subsidies to reduce the budget deficit from roughly 10 percent of GNP to 2 percent or less. The Poles are establishing a social safety net to offset some of the social costs which will result from cuts in subsidies. For these reasons, the new government may need to consider cuts in other areas of the budget to meet their goals in reducing the budget deficit as the program evolves. They may also need to consider accelerating their tax reform initiatives to raise needed revenues.

In reducing the budget deficit and in reducing the rate of credit creation, the Polish Government must maintain sufficient flexibility to avoid a severe recession. While the reform program may cause transitory reductions in real income and higher unemployment, a deep recession would make the government's entire reform program more difficult.

-3-

Exchange Rate Stabilization: Like the distortions produced by subsidies of goods, the current system of multiple exchange rates and complex foreign exchange regulations distorts incentives for exporters and importers and contributes to shortages. The Government of Poland has already begun work on increasing the convertibility and stability of their currency. This is an important step in opening the economy, generating competition and establishing correct relative prices.

The \$1 billion currency stabilization fund, including the U.S. \$200 million contribution, can be a critical asset in helping smooth the transition to a stable and fully convertible currency. The stabilization fund will provide the Polish Central Bank with reserves to establish the credibility of their transitory changes in the value of the zloty. However, the stabilization fund should not be used to defend an exchange rate that is inconsistent with domestic inflation and market conditions. The zloty exchange rate will need to be based on market forces. The fund should be treated as an asset available to offset transitory changes in the value of the zloty, with dollar sales to defend the zloty being offset by subsequent dollar purchases.

Investments in Human Capital: There was a consensus among the group's members that a significant share of U.S. aid should be directed to investments in people, through training. One of Poland's most critical needs is the development of market system oriented expertise in banking, management, accounting, law, marketing and government. The returns to intensive short-term training will make a substantial and lasting contribution to Poland's revitalization and growth. The bulk of this training aid should probably flow through the private sector. For example, the Department of Commerce, with the assistance of the American Association of Public Accountants, has arranged a series of seminars in Poland by leading U.S. accounting firms.

Flexibility in Privatization and Restructuring: Several mission members felt it imperative that the importance of small firms to job growth and innovation be recognized. The United States could assist by providing expertise to help the Poles in developing new laws and modifying existing laws so as to reduce barriers to new firms to a minimum.

In privatizing state monopolies, the Poles would do well to begin by selecting subsets of larger state enterprises, where in-place management and entrepreneurial talent in large existing markets holds promise that the newly privatized enterprise will be successful. The United States

-4-

could provide training and assistance to the Poles to aid them in developing the accounting, legal and financial skills necessary to make sensible economic decisions on which enterprises and factories to shut down and which firms show sufficient promise for restructuring.

With the removal of subsidies, some firms will clearly go bankrupt. It is important that some firms be allowed to go bankrupt so they can be reorganized but, even more important, so a "market test" example is introduced, even if gradually. However, Poland currently does not have the legal infrastructure, commercial codes and bankruptcy laws for such reorganizations to take place. Lacking such laws, it may be imperative that some sort of legal/financial entity be formed to operate and/or restructure failed enterprises. But the government should avoid continuing support to failing and inefficient state enterprises.

Credit, Trade, and Investment Assistance: The Poles need immediate credit assistance to give them some breathing room as they begin to reschedule their debt and reform their economy. The G-24 nations should provide more immediate credit in their proposed aid packages. More efforts should also be made by the Western nations to open their markets to Poland by reducing quotas and other non-tariff barriers to trade.

One of the essential elements in encouraging private investment in Poland will be the reduction in inflation and the establishment of a market-based financial system. However, the U.S. Government could play a vital role by acting as a clearinghouse for information on the rapidly evolving economic situation in Poland. By providing information on the general economic climate, reforms, investment opportunities, and potential investment partners, the United States Government could accelerate investment/joint ventures in Poland.

Summary: Poland presents great opportunities as well as serious economic challenges. By embarking on the course of a private property, market economy, fundamental changes will have to occur in virtually every institution and family in Poland. While a consistent program has been developed in general form -- in a remarkably short period of time -- innumerable details need to be decided, and these will be crucial to the course of the Polish economy. However, the most important element in deciding the success thus far in bringing democracy to Poland suggests that they have the long-run political will and capacity to carry out their economic reforms in the face of great uncertainty, rapid change and possible short-run economic hardship.

Agriculture

I. Assessment

Policies. Development of appropriate agricultural policies is hampered by the lack of infrastructure and the macroeconomic problems of the economy as a whole. Generally speaking, the requisite structures do not exist under which effective agricultural policies can be implemented. These include such basics as general financial and social institutions, legal and accounting and banking structures. Further, there is little that can be done until inflation is brought under control. Similarly, the data base for agriculture that would permit measurement of both needs and performance is lacking.

Food Processing. The country possesses a few excellent facilities, but many oversized, over-centralized and highly inefficient ones. A private alternative to the monopolistic state corporations will need to be built from scratch except in a few areas like cut flowers where liberalization took place a few years ago. The country lacks the essential cadre of middle management and small entrepreneurs (though not entrepreneurial spirit) that will be needed to run smaller, more efficient transportation, storage and processing companies. The net result is great waste which has been estimated to be as high as 30 percent in some years for key crops like potatoes.

Farm Structure. Over two-thirds of Poland's farm area is in private hands with the remainder in large state farms and cooperatives which are state farms by a different name. Farm holdings are highly fragmented with over half the farms smaller than 10 hectares in size, and with these often further divided into diverse plots at some distance from one another. About 30 percent of the population remains employed in farming. Maximum limits exist on farm size of 50 hectares in the better western portion of the country and 100 hectares in the eastern regions. In many cases this precludes full realization of economies of scale.

Production Practices. These vary greatly from archaic to modern and efficient. Most farmers are limited in their access to inputs and appropriate scale farm implements. Mechanization is incomplete as evidenced by the frequency of draft animals. On the other hand, many of the most successful operations are over-capitalized since tractors hold value and currency doesn't. Better balance

-2-

depends on macroeconomic policy. The extension service is viewed by farmers with hostility. Several private producers' organizations (e.g., corn, poultry, swine) are quickly developing and may be the most effective vehicles for improving production practices.

Inputs and Distribution. As with food processing, the distribution and availability of inputs is monopolistic and over-centralized. A single state trading company produces and provides most farm chemicals, and another handles implements. The need for decentralizing is obvious, but the success of an attempt to do so is uncertain. Again, a purely private alternative needs to be developed. Access is costly in money and time: a day a week is spent by farmers in lines or tied up in searching for farm needs. Traditionally most inputs have gone to the smaller public sector with the majority of private farms starved for them. There has been no market to establish true demand.

Finances. Farms, including the success cases, are cash operations. Indeed, effective use of farm credit must await stabilization of the currency. Many successful farmers drive their product hundreds of miles west to markets in West Berlin or West Germany, obtaining hard currency to purchase their most urgent needs in the West. Those that market their products in Poland immediately reinvest revenues in land, equipment or, when all else fails, housing for their families. There is demand for rural non-farm credit by entrepreneurs who want to start marketing, distribution and processing operations on a small-scale basis. But until the macroeconomy is better balanced, it will be nearly impossible to determine true efficiencies in all rural enterprises, or for them to develop to their full potential.

Machinery. Poland produces a good, medium-sized tractor that is suitable for its (by U.S. standards) small farms, but little else in the way of implements and machinery seems to be in satisfactory supply including spare parts for the tractors. Even what is available is often too expensive for most farmers. As noted above, mechanization is not complete, and there seem to be big disparities among marginal and successful farms.

II. Recommendations

Policies. Most important, Poland must get its macroeconomic situation under control. It needs to limit

-3-

inflation and make the currency convertible. Only afterwards will sound agricultural policies work. Some general guidelines are clear: subsidies anywhere in the farm/food system should be eliminated; input supplies and pricing will be critical to output, and this may be one of the few places where it makes sense to gradually move toward world price levels; tax incentives may be beneficial for start-up businesses in rural areas and for joint ventures in the input and food processing sectors. Closely related to policy formation is the need to develop at a minimum three kinds of reliable data bases: for prices received by farmers, for profit margins at all points in the marketing chain, and for food expenditures by socioeconomic group.

Food Processing. Monopolies need to be broken and existing state firms need to be downsized and privatized. In a country where investment capital is scarce, it may make more sense to develop leasing arrangements than selling off all companies immediately. More importantly, a purely private alternative system needs to develop to compete with the old, established companies. This sector also needs reliable market information. To provide the necessary managerial skills for free market operations, internships in western companies may be highly effective.

Farm Structure. There is a gradual trend towards increasing farm size. The country is showing the sort of bipolar development seen in the late 1940's in West Germany as farms either become large enough to be truly competitive, or become distinctly part-time operations. In view of the unemployment that will be inevitable in urban areas over the next few years, it would be inappropriate and premature to purposely accelerate these trends in a way that would also decrease on-farm employment. Rather, as price adjustments occur and better indications of true farm efficiencies emerge, these structural trends are likely to speed up by themselves. Decentralization of input supply and processing industries should provide more off-farm employment in rural areas.

Production Practices. The most important steps that can be taken to encourage improved practices are to establish correct economic incentives, to increase the supply and widen/privatize the distribution of inputs, and to develop an effective extension system that is trusted by producers. Providing help in setting up and implementing an extension system should be a high priority for foreign assistance.

Inputs and Distribution. The United States, through public/private cooperation, should strive to supply as much as possible of the chemical input request the Delegation received. This effort can be coordinated with the G-24 assistance group. The United States can also supply (is supplying) much of the needed feed inputs through its food aid programs. Future "food aid" should be confined to feeds unless unforeseen food needs develop over the next few years until Poland's own agricultural productivity is higher. An important aspect of providing this assistance is the distribution mechanism within Poland. To some degree the existing state company, CIECH, is the only effective mechanism, yet based on past experience it does not reach all farmers effectively. Relationships with private groups like the Water Supply Foundation and Foundation for the Development of Polish Agriculture, perhaps in conjunction with the private producers' organizations, should be explored. Longer term, input supply and distribution may be an attractive area for joint venture investment.

Finance. High priority should be accorded to the provision of rural credit, especially for nascent entrepreneurs in the areas of distribution, transportation, marketing and processing of inputs and food. Eventually, farm credit will also become popular as farmers seek to mechanize or increase their farm sizes. A real banking system is needed to replace the ineffective present one where simple bank transfers can take months. The ultimate effectiveness of a credit system, however, depends on getting the macro problems of inflation and nonconvertibility corrected. Some rural credit needs will be for hard currency as well as zlotys. As that process occurs, other financing mechanisms like debt-equity swaps for joint venture investment in larger scale operations will also make sense.

Machinery. The needs here are similar to those with respect to inputs and food processing. First, a true market needs to develop, allowing farmers to indicate their needs rather than being presented with inappropriate choices. Investment in the manufacture and distribution of implements and machinery will be needed, and this is another area to be studied by the U.S. private sector for possible joint venture investment. Given farm sizes, it may be that the scale of West European equipment is more suitable for Poland's farmers than American.

Services. There is no telecommunication system in rural Poland. Special mobile radio service systems and products could be utilized to improve the productivity of farmers, as could a phone system. Efforts should be considered to evaluate the establishment of one or more rural telecommunication services in Poland. In rural villages in the United States a private sector entity

-5-

typically provides storage capacity for surrounding farmers, drying facilities for their products, often a market for those products, and often also a source of supply for inputs such as fertilizer, herbicides, and pesticides. That is the heart of the American agricultural system. We should help the Poles try out models of this nature, either through organizing farmer cooperatives or by stimulating small business ventures to fill this need. One of our Mission members has offered to accept potential Polish entrepreneurs into a training/business exposure program that could be very helpful in this regard.

Training. To improve agricultural productivity in Poland, agricultural training programs should be given greater emphasis. Business and economic scholarships provided under the U.S. economic assistance plan for Poland could be expanded to include scholarships for agribusiness, agronomy, and related sciences. Not only should there be training in various agricultural subjects, but also in-depth training for farm managers, storage and transportation specialists, and mechanics.

Port Facilities. We need further evaluation, and perhaps a feasibility study of the potential for Poland to provide a major port facility for Eastern Europe, a function now heavily dominated by ports such as Rotterdam and Hamburg. If feasible, this could be a major source of earnings for Poland, and it could become the commercial gateway to this part of the world.

Other. In the course of our discussions we developed a tacit awareness of the looming problem of increasing unemployment and increased hardship among some groups because of the great increase in food prices. The development of a safety net to extend to rural as well as urban populations is clearly necessary at an early stage in structural readjustment. We should also quickly study the possibility of using local proceeds from food aid sales to assist vulnerable groups. To make the transition easier, one private sector representative suggested that the United States provide a permanent senior advisor to Poland's Minister of Agriculture.

Commerce and Industry

A. Assessment

As one would expect, the new Polish Government faces tremendous challenges in implementing its reform, modernization and privatization measures. Following six years of World War II devastation and 45 years of Communist mismanagement, nearly 90 percent of Polish industry still operates as a state-owned enterprise. Nevertheless, there is real hope. The Polish people are determined to rebuild the economy. Their genuine spirit and inherent and acquired skills are an inspiring resource.

Industrial plants are old, obsolete and technologically unsophisticated. Research and development is extremely limited. Economic conditions are daunting, with hyperinflation, large foreign debt and wage indexation. Environmental and worker health and safety matters have been noticeably neglected. The country has a long record of bloated, inefficient bureaucracy. Poland must now devise and implement market reforms, cost controls and modern management. The new administration of young, hopeful, daring leaders is determined to turn things right side up, and these leaders appear to have the support of the people. It will be difficult to tackle any one of these problems in the short term, but the government must work on all simultaneously, enormously increasing the difficulty of the task.

Poland needs to build a contemporary infrastructure and develop a set of tools to create a market economy. Banking, telecommunications, distribution systems and pollution control technologies are high priorities. For many industries, the Poles understand the problems, have a general plan to remedy the situation, but need help in the implementation. The country needs legal and accounting systems and financial markets.

Poland especially needs an accounting system in the broadest sense as well as the specific discipline. In an economic system in which institutional shortfalls have for many years been made up by subsidies, it is vitally important that systems which reflect true costs are put in place. It is impossible to allocate scarce resources properly when true costs do not guide decisions.

Poland's telecommunications system is among the least advanced in the industrialized world, with only 1 percent of rural homes and 10 percent of urban homes receiving service. Only one-third of all domestic or

international calls are completed. The Polish Government is committed to a bold plan to rebuild Poland's telecommunications infrastructure, to strengthen private sector manufacturing capability and to overhaul the regulatory regime. However, capital is scarce. The U.S. Government's goal should be to supplement the obvious technical assistance needed to help rebuild this critical element of Poland's economic infrastructure along more market-based lines. This will involve reviewing export control limits.

The new leadership is now putting the final touches on an ambitious legislative package constituting a comprehensive economic restructuring program. The Poles expressed an interest in U.S. comments on their package, both in terms of macroeconomic policy and of the legal conditions for the economic restructuring. The Polish Cabinet will present this entire package to the Parliament in time for adoption by January 1, 1990. The U.S. drafts for a comprehensive Business and Economic Agreement, presented by Secretary Mosbacher in Warsaw, are designed to produce an agreement that will attract U.S. investment.

The country needs assistance to provide management training and develop modern engineering skills. Because the environment is in a terrible state, the Poles need to implement new projects so as to achieve a sustainable net environmental gain.

One of the most important needs facing Poland is that of management training. No amount of financial or other assistance can succeed in turning Polish industry around without a substantial transfer of management techniques to Polish industry. Put simply, most Polish managers do not know how to organize resources and run efficient operations based on market pricing. It is critical that this training gap be overcome.

An extremely successful operation in the 1950's and 1960's provides a model which could be followed -- the "Japan Productivity Center." This center was established at U.S. initiative in 1955 and was funded as a joint American-Japanese endeavor. It's primary function was to bring Japanese managers to American factories to learn American management techniques. Over 12,000 Japanese managers visited U.S. plants under this program, learning production, financial, marketing, and other managerial skills by first-hand observation. Upon their return to Japan, they conducted seminars to teach their fellow managers what they had learned.

A similar center could be established for Poland, perhaps called the "Polish-American Productivity Institute" (PAPI), which would bring Polish managers of all levels to the United States for on-the-job training to learn how to manage in a private sector environment.

In all of Poland's priority areas, U.S. companies are leading global competitors. We must encourage U.S. firms to take advantage of current opportunities to become involved in Poland's new economy from the start. Poland is a trend setting country. President Jaruzelski told the delegation that he wants economic and political freedoms in Poland to be "contagious." U.S. firms should take appropriate positive risks which will require only modest investment to advance these market reforms. Moreover, many Poles expressed strong interest in having U.S. companies involved.

However, one of the key hurdles facing U.S. companies who want to assist Poland build up its infrastructure is export controls. In light of the democracy movement, the U.S. Government must carefully review its export control policy towards Poland.

It is important that the Polish people strengthen and broaden their political and economic reforms by achieving tangible success on certain carefully selected initial demonstration projects. U.S. companies can assist the Poles to prove that market reforms can work. It is essential to instill a popular concept that these changes will take time and will come only after learning from many mistakes.

B. Recommendations

1. Conclude negotiations as soon as possible on a business and economic agreement that will provide a basis for increased U.S. direct investment, through investment protection assurances, intellectual property protection, and business facilitation measures.
2. Concentrate financial and technical assistance initially on several critical industry sectors: banking, medium-sized agriculture and industrial projects, telecommunications, road building, rail transport, and pollution control and environmental services. Fulfill terms of the Joint Communique on telecommunications by formalizing a cooperative working relationship to assess Poland's infrastructure needs and to provide advice on telecommunications regulations and technologies.

3. Begin operations for the Enterprise Fund immediately. Include representation and input from the Polish private sector. Establish an information and project evaluation office in Poland.
4. Instruct Commerce, Overseas Private Investment Corporation (OPIC), Trade Development Program (TDP) and other agencies to organize information seminars in Poland and Washington on available resources including the Support for East European Democracy (SEED) legislation signed by President Bush on November 28. Develop and encourage private sector contacts needed to implement the legislation.
5. Organize and conduct a legal seminar in conjunction with the Government of Poland. The seminar would include senior lawyers from both government and U.S. corporations interested in doing business in Poland. U.S. lawyers would provide input on subjects such as antitrust and unfair competition, protection for intellectual property, securities, contracts and forms of business organization, as well as trade laws.
6. The Polish Government has expressed a willingness to implement a security safeguard system for export controls. The United States and COCOM should work with Poland to achieve this objective. In exchange for a Polish commitment to implement specific safeguards, the United States and COCOM should establish a policy of "favorable consideration" for certain key products and industries such as telecommunications, transportation and banking. The policy could be expanded as Poland develops a successful track record on export controls.
7. Develop government and private sector exchange programs to provide Polish private sector representatives management and technical training. For example, CEOs from the delegation have offered to train Poles at their companies' facilities located in the United States and Europe. As an important first step, the International Executive Service Corps has placed ten U.S. executives with firms in Poland. Additional Enterprise Fund support would enable this number to be greatly expanded. Implement the U.S. Telecommunications Training Institute's specialized training program for Poland. The training is provided at U.S. corporate sites.

8. Establish a Polish-American Productivity Institute (PAPI) to assist Polish enterprises in becoming more productive by sending teams of Polish managers to the United States to study U.S. methods. The Polish businesses would fund the managers' travel expenses to and from the United States. PAPI would act as the broker/clearinghouse, finding U.S. businesses to sponsor the Polish managers. The sponsoring business would fund the living expenses of the manager while he/she was "in-training" at that firm. The managers would then return to Poland to apply what they have learned at their individual enterprises. The SEED program may be able to provide some financial support.
9. Consider sending teams of U.S. experts from a variety of industries to help develop national policy plans and business plans. Five examples might be energy, environment, agribusiness, transportation, and tourism. Another example could be a privatization team to work on one or more of the initial state enterprises scheduled for privatization. Included among the energy issues for consideration are: reliance on coal for export revenues, pollution abatement, substitutability of natural gas, the rational pricing of energy to encourage conservation and more efficient production usage of energy.
10. Consider new priorities for environmental initiatives. For example, a fluidized bed technology project in the Silesia region is likely to have a greater positive impact than some other projects that have been discussed. Substantial improvement can be obtained through a modest, well-planned construction program for the processing of raw sewerage and, at least, primary treatment of industrial wastes. In addition to the reconstruction program, there needs to be a series of demonstration projects (some now under consideration in the recent EPA bilateral agreement) to install primary controls for the most extreme cases of air and water pollution.
11. Encourage Polish Government to modify its investment regime to create more attractive and competitive conditions for Western companies. Clarify foreign ownership in telecommunications service and manufacturing projects.
12. Expand Department of Commerce personnel in Warsaw, specifically the Foreign Commercial Service.

13. Encourage the Polish Government to establish an agency to play a clearinghouse role to coordinate foreign business investment interests.
14. Finally, the constant thread is that Poland desperately needs private sector expertise and specific bottom line oriented experts in all areas of business. U.S. assistance efforts should include bringing in U.S. experts proficient in many businesses.

Labor

The working men and women of Poland are responsible for the fundamental changes under way in Poland today. The success of the ambitious Polish economic program currently being undertaken depends on the Polish people's continued support for the Government and their tolerance of the effects of economic reform. Furthermore, the long-term prosperity of the Polish economy will depend, in large measure, on the manner in which Poland uses its single most valuable resource -- its workforce.

The transition from a centralized economy to a market economy, will cause hardships for workers. As the growth of monetary wages is slowed, as subsidies on State enterprises and consumer products are reduced, and as State firms are privatized, streamlined, or closed, there will be reductions in real wages and unemployment. While it is essential that measures to halt inflation and stabilize the currency be taken quickly, the Government must have an adequate social policy in place to deal with anticipated worker displacement and adjustment. If the social issues related to economic reform are not addressed promptly and adequately, the potential for worker dissatisfaction and unrest will be high and could undercut the difficult reforms that are needed to assure long-term economic success.

ASSESSMENT

The Labor Sector Team met with a broad group of government officials, including Minister of Labor and Social Policy Jacek Kuron and other economic ministers, members of the Sejm, leaders of the Solidarity Union, students in a labor training facility, workers, management in large and small enterprises, and the general public.

We were impressed with the level of support for the Solidarity-led government, the widespread commitment to democracy and pluralism, the knowledge and pride of Polish history, and the positive response thus far to the Government's call for self-help and voluntarism. Government officials, workers, and union members alike spoke assuredly of the self-reliance of the Polish people and of their capacity to endure the hardships of reform.

The Polish Labor Force: Our preliminary perceptions regarding the Polish labor force were largely validated by the findings of our mission. Poland can take heart in the fact that its labor force is young, growing, well educated,

and well trained: the percentage of workers under the age of 40 is greater than in any other Western industrialized nation; literacy is nearly universal; and, approximately half of Poland's workers have technical or trade school training beyond the 8-year mandatory education level.

The performance of Poland's workforce, however, reflects the effects of a Communist economic system. A fixed wage structure and barriers to labor mobility sharply restrict work incentives, resulting in low productivity. The introduction of free enterprise wage incentives, accompanied by opportunities for worker mobility, should increase individual work effort and cause substantial productivity gains. The key will be to maintain the support of workers for reform during the difficult early days of transition.

Effects of Economic Reform on the Labor Force: The Polish Economic Reform Plan calls for severe curtailment of subsidies to state enterprises, extensive restructuring and privatization, and the elimination of unprofitable enterprises. These actions, if taken with sufficient force to curtail inflation and create an adequate environment for Western private investment, are likely to result in more unemployment and worker dislocation than some currently anticipate.

Minister of Labor and Social Affairs Kuron spoke of his dislike for the word "unemployment." He indicated, however, that as many as one-half of the Polish work force will likely take new jobs in a free enterprise economy. He distinguished between those transitioned smoothly to new jobs and those left out of work, i.e., the "unemployed."

We were struck by the fact that many areas of high priority need in Poland will require simultaneous action on many fronts. For example, Poland's serious housing shortage is a major barrier to labor mobility and worker adjustment. Although we propose to offer craft skills training in the housing area as part of a targeted program of technical assistance to Poland, a system-wide approach to the housing problem is clearly needed. In addition to skills training,

reform in land use laws and regulations, access to credit and home mortgages, and the elimination of barriers to the distribution of building materials are important to addressing the housing shortage.

A Social Shield: The Polish Government is aware of the need for what they term a "social shield" to cushion workers during the transition to a free enterprise system. Under the State-directed economic system, a wide array of social benefits, e.g., housing, medical services, pensions, access to vacation resorts, etc., have been tied to employment in State enterprises. If workers are displaced from these positions, they stand to lose much more than their wages. Until a safety net is designed and implemented, displaced workers will not have access to the kinds of social services -- including unemployment compensation -- customarily available in Western economies. The Government is aware that without these services, serious worker unrest could result. They have, therefore, given high priority to the early establishment of an effective "social shield" in addition to near-term improvement in standards of living.

RECOMMENDATIONS

The U.S. Department of Labor proposes a targeted program of technical assistance to Poland, with the majority of the program to be delivered in Poland. We will begin to implement the program immediately in accordance with the broad outlines of the Memorandum of Understanding signed by Secretary Dole and Minister Kuron on November 30, 1989. Major elements of the Department's program will include:

- o Business Training: Development of a program focused on the basic managerial and entrepreneurial skills that will be essential in Poland's emerging market environment. This program will concentrate on a broad array of fundamental skills in areas such as business organization, personnel, accounting, capital and income budgeting, marketing, wholesaling, distribution, and retailing. As the Polish economy expands, we may offer sector-specific business training programs in areas such as the banking sector (identified as a high priority by the Poles).
- o Unemployment/Employment Services: Polish officials have given high priority to the establishment of an effective "social shield" to protect workers and their families during economic restructuring. The Department of Labor will provide technical assistance in devising and implementing a workable unemployment compensation and an employment services system. We will explicitly refrain, however, from advising the Poles on policy issues, e.g., levels and duration of benefits.

-4-

- o Labor Statistics: Sound statistical information on matters such as employment, wages, prices, and productivity will be essential to the efficient functioning of Poland's free enterprise economy and to the attraction of foreign investment. Consequently, the Department of Labor will provide technical assistance in the development and operation of needed statistical information systems similar to those operated in the United States by the Department's Bureau of Labor Statistics.
- o Crafts Training: To help Poland's housing shortage and alleviate a major impediment to increased labor mobility, the Department will work with the AFL-CIO on the development and delivery in Poland of a crafts training program in the building and construction trades. As this program evolves, skills training to support other priority sectors of the Polish economy will be considered.

We are working with the Polish Government to establish a Polish-American Labor Institute in Warsaw. This Institute will serve as a center for the planning and delivery of assistance and as a visible symbol of American presence in Poland.

In addition to the program outlined above, we recommend that the World Bank accelerate its consideration and delivery of structural adjustment assistance to Poland. Prompt approval of this loan will produce zloty offsets that the Poles could use in the near term to fund its planned unemployment compensation system. This action seems crucial given the Government's intention that a proposed employment tax to fund unemployment insurance not go into effect until late next year, at the earliest.

It would be inappropriate to report on the labor situation in Poland without reference to both the significant accomplishments and the continuing needs of the trade union NSZZ Solidarnosc. The union has requested technical assistance and training from the United States in areas such as collective bargaining and dispute resolution techniques; labor market analysis; worker safety and health; the translation of labor materials; and union administration. Labor Ministry officials, and Dr. Cooper of Upjohn, also stressed the importance of making steady improvement in the area of worker safety and health. This is clearly an area that will deserve increased attention as reform progresses.

To the extent feasible, the Department of Labor will ensure that Solidarnosc and its members are fully involved in our programs of assistance to Poland. However, many of their specific requests will need to be addressed by the AFL-CIO

